



# **TAX BULLETIN 03-1**

## ***Virginia Department of Taxation***

February 18, 2003

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### **IMPORTANT INFORMATION REGARDING** **2001 AND 2002 VIRGINIA INCOME TAX** **RETURNS AND CERTAIN VIRGINIA ESTATE** **TAX RETURNS**

#### **VIRGINIA INCOME TAX FIXED-DATE CONFORMITY ADVANCED TO DECEMBER 31, 2002**

*Under emergency legislation passed by the 2003 General Assembly and signed by Governor Warner, Virginia's fixed-date of conformity to the terms of the Internal Revenue Code has been advanced from December 31, 2001 to December 31, 2002. However, the special 30% bonus depreciation and the 5-year net operating loss carryback enacted under the Job Creation and Worker Assistance Act of 2002 are not included in this change. This notice is intended to provide taxpayers with directions on how to reconcile this legislation on their 2001 and 2002 Virginia income tax returns.*

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Effective for taxable years beginning on and after January 1, 2001, Virginia's fixed date of conformity to the terms of the Internal Revenue Code is advanced from December 31, 2001 to December 31, 2002, with two exceptions. Virginia will not conform with the federal tax provisions allowing the special 30% bonus depreciation and the 5-year net operating loss carryback. However, Virginia will conform to all other previously enacted provisions under federal income tax law.

The fixed-date conformity adjustments that will be no longer required when filing a 2002 tax return are those related to:

#### **Individuals and Fiduciaries**

- Educator Expenses
- Qualified Disaster Relief Payments
- Certain Disability Income
- Employer-Provided Death Benefits
- Clean Fuel Vehicle Deduction
- Foster Care Payments
- Subchapter S-Corporation Discharge

**Fiduciaries Only**

Personal Exemptions for Certain Disability Trusts

**Corporations**

Clean-Fuel Vehicle Deduction

S-Corporation Discharge

**Estates**

Tax relief for victims of terrorism

**VIRGINIA INCOME TAX**

Since 1972, Virginia has conformed to federal income tax law. Whenever federal income tax law was changed, the changes automatically affected Virginia income taxes, unless otherwise exempted. In 2002, a provision was enacted that fixed Virginia's conformity to Internal Revenue Code terminology to the Internal Revenue Code as it existed on December 31, 2001. Because of changes in federal law contained in the Victims of Terrorism Act of 2001 and the Job Creation and Worker Assistance Act of 2002 effective for 2001, some taxpayers would have had to make adjustments to their federal adjusted gross income or federal taxable income through the fixed-date conformity adjustments on the 2002 income tax return. Some adjustments were also made on 2001 income tax returns. This bulletin will instruct taxpayers about which fixed-date conformity adjustments are still necessary for both 2001 and 2002 income tax returns, if applicable.

Most Virginia taxpayers will not be affected by this change because only a limited number of taxpayers would have been required to make the special, fixed-date conformity adjustments on Schedule ADJ.

**Special Instructions for Taxpayers**

***Taxpayers Who Have Not Yet Filed***

**Individuals**

Individuals who have a special, fixed-date conformity adjustment for bonus depreciation are still required to make the corresponding adjustments that are located on Pages 14 and 15 of the instructions for Form 760. In addition, if the federal bonus depreciation has an effect on any other item included in federal adjusted gross income, an adjustment is still required to be made as either an addition on Line J. of Page 14 of the instructions for Form 760 or as a subtraction on Line C. of Page 16 of the instructions for Form 760. All individuals with a fixed-date conformity adjustment will still be required to complete the Fixed-date Conformity worksheet on Page 9 of the Form 760 Instructions.

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The fixed-date conformity provisions that individuals should disregard are provisions that would have prohibited Virginia income taxpayers from enjoying certain newly-enacted federal tax relief provisions on their Virginia return. These tax relief provisions, that are new for 2002, include:

- The new Educator Expense deduction,
- Expanded definitions of disability income and foster care payments that are not subject to income taxation,
- The exclusion of qualified disaster relief payments and employer-provided death benefits from income taxation, and
- The delay of the phase-out of the clean-fuel vehicle deduction.

All of these tax relief provisions will now be allowed to flow through to the Virginia individual income tax return as a result of the emergency legislation. Therefore, individuals who have not yet filed their income tax returns can disregard the following special, fixed-date conformity additions located on Page 14 of the instructions for Form 760:

- B. Qualified Disaster Relief Payment**
- C. Certain Disability Income (Part 1)**
- D. Certain Disability Income (Part 2)**
- E. Employer-Provided Death Benefits**
- F. Educator Expenses**
- G. Clean-Fuel Vehicle Deduction**
- H. Foster Care Payments (Part 1)**
- I. Foster Care Payments (Part 2)**

Also, individuals who have not yet filed their income tax returns should disregard the special, fixed-date conformity subtraction for a “**Subchapter S Corporation Discharge**” located on Pages 15-16 of the instructions for Form 760.

For individuals who must file either a Form 760PY Part-Year Resident Individual Income Tax Return or a Form 763 Nonresident Individual Income Tax Return, all of the changes explained above for individuals will apply. The corresponding fixed-date conformity instructions for part year residents are located on Pages 14 through 16 of the Form 760PY Instructions. The corresponding fixed-date conformity instructions for nonresidents are located on Pages 11 through 13 of the Form 763 Instructions.

### **Corporations**

Corporations that have not yet filed their income tax returns should only make special, fixed-date conformity adjustments relating to the special 30% bonus depreciation. Adjustments relating to the special 30% bonus depreciation are entered on Lines 2 and 4 of Form 500 and explained on Page 4 of the Form 500 and 500S instructions. In addition, if the federal bonus depreciation has an effect on any other

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item included in federal taxable income, an adjustment is still required to be made as either an addition on Line 2b of Form 500 or as a subtraction on Line 4b of Form 500.

For Form 500S, adjustments relating to the special 30% bonus depreciation are described on Pages 7-8 of the Form 500 & 500S instructions. The adjustments relating to the special 30% bonus depreciation are entered on lines 2a, 2b, 4a, and 4b of Form 500S. In addition, if the federal bonus depreciation has an effect on any other item included in federal taxable income, an adjustment is still required to be made as either an addition on line 2d or as a subtraction on line 4d of Form 500S.

**Fiduciaries**

Fiduciaries who have a special, fixed-date conformity adjustment for bonus depreciation are still required to make the corresponding adjustments that are located on Page 8 of the instructions for Form 770. In addition, if the federal bonus depreciation has an effect on any other item included in federal taxable income, an adjustment is still required to be made as either an addition on Line K. of Page 8 of the instructions for Form 770 or as a subtraction on Line C. of Page 8 of the instructions for Form 770.

The fixed-date conformity provisions that fiduciaries should disregard are provisions that would have prohibited Virginia income taxpayers from enjoying certain newly-enacted federal tax relief provisions on their Virginia return. These tax relief provisions, with one exception, are the same as those identified for individuals. The exception is that fiduciaries may also disregard the fixed-date conformity addition for **“Personal Exemption for Certain Disability Trusts.”** This fixed-date conformity addition plus all of the same additions identified for individuals are located on Page 8 of the instructions for Form 770. Therefore, fiduciaries who have not yet filed their income tax returns should disregard these special, fixed-date conformity additions.

Fiduciaries who have not yet filed their income tax returns should also disregard the special, fixed-date conformity subtraction for **“Subchapter S Corporation Discharge”** that is located on Page 8 of the instructions for Form 770.

**Individuals & Corporations Schedule CR**

Individual taxpayers who claim the Clean-Fuel Vehicle and Certain Refueling Property Tax Credit should not make the fixed-date conformity adjustment on Line 30a on Page 2 of Schedule CR. On Line 30a on Page 2 of Schedule CR, all individual taxpayers should instead enter the same amount entered on Line 30. Corporations who claim the Clean-Fuel Vehicle and Certain Refueling Property Tax Credit should not make the fixed-date conformity adjustment on Line 35a of the Form 500CR. On Line 35a, all corporate taxpayers should instead enter the same amount entered on Line 35.

### **Treatment of the 5-Year Net Operating Loss Carryback**

The treatment of any 5-year net operating loss carryback is not affected by the passage of the 2003 legislation. All taxpayers should follow the instructions given in Virginia Tax Bulletin 02-3 regarding any necessary adjustment for a 5-year net operating loss carryback.

#### ***Taxpayers Who Have Already Filed***

##### **Individuals**

Individuals who have already filed a 2002 individual income tax return with a fixed-date conformity adjustment that is not now required should file an amended 2002 Virginia individual income tax return. Amended individual income tax returns are filed using the 2002 Form 760 by filling in the oval at the top of Page 1 to indicate that the return is an amended return. Taxpayers should fill out the form completely and disregard those fixed-date conformity additions and subtractions explained above. Also, any taxpayer filing an amended return should follow the special instructions for amended returns on Page 21 of the Form 760 Instructions.

For nonresidents, instructions for filing an amended return are found on page 18 of the Form 763 Instructions. Instructions for part-year residents filing an amended return are found on page 22 of the Form 760PY Instructions.

##### **Corporations**

Corporations that have already filed a 2002 corporation income tax return with a fixed-date conformity adjustment that is not now required should file an amended 2002 Virginia corporation income tax return.

For Form 500 filers, amended returns are filed using Form 500X, the Amended Virginia Corporation Income Tax Return. Corporate income taxpayers should follow the instructions for Form 500X and recompute the proper fixed-date conformity adjustment, if any, and report the corrected amount as a change in Net Virginia Modifications on Line 2, Column B.

For Form 500S filers, amended returns are filed using the Form 500S with the word "AMENDED" written at the top of the return. Taxpayers should fill out the form completely as if it were the original return and recompute the proper fixed-date conformity adjustments explained above.

##### **Fiduciaries**

Fiduciaries who have already filed a 2002 fiduciary income tax return with a fixed-date conformity adjustment that is not now required should file an amended 2002

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Virginia fiduciary income tax return. Amended fiduciary income tax returns are filed using the 2002 Form 770 with the word "AMENDED" written at the top of the return. Taxpayers should fill out the form completely as if it were the original return and recompute the proper fixed-date conformity adjustments explained above.

**2001 Amended Returns**

If you filed a 2001 Virginia income tax return for an individual, S corporation, or fiduciary with an adjustment for fixed-date conformity, you may need to file an amended return. If the fixed-date conformity adjustment was for either the special 30% bonus depreciation or the 5-year net operating loss carryback, you do not need to file an amended return. If the fixed-date conformity adjustment was for Subchapter S Corporation Discharge of Indebtedness, you should file an amended return that removes this adjustment. This adjustment was previously explained in Virginia Tax Bulletin 02-3.

For **individuals**, 2001 amended individual income tax returns are filed using the 2001 Form 760 by filling in the oval at the top of Page 1 to indicate that the return is an amended return. The 2001 Form 760 is available on the Department of Taxation's website at <http://www.tax.state.va.us>. Taxpayers should fill out the form completely and not include a fixed-date conformity adjustment for a Subchapter S Corporation Discharge of Indebtedness. Also, any taxpayer filing an amended return should follow the special instructions for amended returns on Page 21 of the 2001 Form 760 Instructions.

For part-year resident individuals, 2001 amended individual income tax returns are filed using the 2001 Form 760PY. Instructions for filing an amended return are found on page 21 of the 2001 Form 760PY Instructions. For nonresident individuals, 2001 amended individual income tax returns are filed using the 2001 Form 763. Individuals should follow the instructions for filing an amended return found on page 18 of the 2001 Form 763 Instructions. These 2001 forms are available on the Department of Taxation's website at <http://www.tax.state.va.us>.

For **corporations** that filed a Form 500 in 2001, the filing of an amended return will not be necessary. Amended returns will be necessary for S corporations with a fixed-date conformity adjustment for a Subchapter S Corporation Discharge of Indebtedness. S corporations may amend their 2001 return by filing the Form 500S with the word "AMENDED" written at the top of the return. The 2001 Form 500S is available on the Department of Taxation's website at <http://www.tax.state.va.us>. Taxpayers should fill out the form completely as if it were the original return without the fixed-date conformity adjustment for a Subchapter S Corporation Discharge of Indebtedness and recompute the proper fixed-date conformity adjustments explained above.

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For **fiduciaries**, 2001 amended fiduciary income tax returns are filed using the 2001 Form 770 with the word "AMENDED" written at the top of the return. The 2001 Form 770 is available on the Department of Taxation's website at <http://www.tax.state.va.us>. Taxpayers should fill out the form completely as if it were the original return without the fixed-date conformity adjustment for a Subchapter S Corporation Discharge of Indebtedness.

**VIRGINIA ESTATE TAX**

Passage of this emergency legislation also provides estate tax relief for the estates of victims who died in 2001 by conforming to the provisions of the federal Victims of Terrorism Tax Relief Act of 2001. The federal act provides a reduced estate tax rate schedule under Internal Revenue Code section 2201(c) that is applicable to estates of victims of the September 11, 2001 terrorist attacks. Using this schedule, a taxable estate of \$2,936,818 or less is exempt from federal and Virginia estate tax because the federal unified credit of \$220,550, applicable to estates of those who died in 2001, offsets the federal and Virginia tax.

Estates of victims who died in 2001 that have already filed a Virginia estate tax return may file an amended estate tax return to claim a refund as a result of Virginia's conformity to this provision. To file an amended estate tax return, taxpayers should file a Virginia Estate Tax Return, Form EST-80, with Box D ("Amended Return") checked at the top of the return. The Form EST-80 is available on the Department of Taxation's website at <http://www.tax.state.va.us>.

If you have any additional questions, please contact us at (804) 367-8031 for individual income tax questions or (804) 367-8037 for corporate income tax questions, or visit our website at <http://www.tax.state.va.us>.